

Message Text

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ACTION EB-11

INFO OCT-01 ARA-16 EA-11 ADP-00 EUR-25 CIAE-00 DODE-00

PM-07 H-03 INR-10 L-03 NSAE-00 NSC-10 PA-03 RSC-01

PRS-01 SS-15 USIA-15 AGR-20 COME-00 LAB-06 STR-08

TRSE-00 CIEP-02 OMB-01 RSR-01 /170 W

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R 011830Z AUG 73

FM AMEMBASSY MANAGUA

TO SECSTATE WASHDC 2127

INFO AMEMBASSY GUATEMALA

AMEMBASSY SAN JOSE

AMEMBASSY SAN SALVADOR

AMEMBASSY TEGUCIGALPA

AMEMBASSY TOKYO

C O N F I D E N T I A L SECTION 1 OF 2 MANAGUA 3297

GUATEMALA FOR ROCAP

E.O. 11652: GDS

TAGS: EAGR, BDIS,NU

SUBJECT: U.S. BROKER CONCERNED COTTON PRICES WILL

AFFECT FUTURES DELIVERIES

BEGIN SUMMARY: MR. JACK WILSON OF WIEL BROTHERS,
MEMPHIS, TENNESSEE, ACCOMPANIED BY HIS LCAL AGENT,
CALLED ON AMBASSADOR JUNE 30 TO EXPRESS HIS
APPRECIATION FOR OUR EARLIER ASSISTANCE IN RESOLVINGZJ
DISPUTE OVER PAYMENT OF EXPORT TAX ON COTTON
(MANAGUA 1788)AND TO APPRISE AMBASSADOR OF POTENTIALLY
DIFFICULT SITUATION DEVELOPING IN THE COTTON TRADE AS
A RESULT OF SKYROCKETING COTTON PRICES AND THE DOLLAR
DEVALUATION. HIS PRICIPAL CONCERN IS THAT RISING
WORLD COTTON PRICES WILL CAUSE GROWERS WHO WROTE
EARLY FUTURES CONTRACTS AT LOWER PRICES TO EITHER NOT
DELIVER OR TO BRING STRONG PRESSURE ON GOVERNMENTS TO
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VOID EXISTING CONTRACTS AND LEGISLATE A RETROACTIVE,

MINIMUM EXPORT PRICE. ACCORDING TO WILSON, THESE PRESSURES EXIST IN VARYING DEGREES IN ALL CENTRAL AMERICAN COUNTRIES. HE FELT THEY WERE STRONGEST IN GUATEMALA AND WEAKEST IN EL SALVADOR, WITH NICARAGUA IN THE MIDDLE. THE PROBLEM FOR WIEL BROTHERS AND OTHER U.S. BROKERS IS THAT THEY HAVE ALREADY SOLD MOST OF THEIR FUTURES CONTRACTS TO CUSTOMERS IN JAPAN WHICH TAKES ROUGHLY 70 PERCENT OF CENTRAL AMERICAN PRODUCTION. END SUMMARY.

1. IN THE CASE OF NICARAGUA, FOB FUTURES PRICES FOR THE 1973/74 CROP HAVE RISEN FROM A STARTING POINT OF \$30 PER CWT TO A CURRENT \$52 PER CWT, AND INCREASE OF OVER 70 PERCENT. A RECENT SURVEY OF LOCAL BROKERS SHOWS TOTAL FUTURES SALES AMOUNT TO 396,000 BALES (500 LBS). WITH AN AVERAGE CONTRACT PRICE BETWEEN \$34 AND \$36 PER CWT. TOTAL PRODUCTION FOR 1973/74 IS ESTIMATED AT ROUGHLY 550,000 BALES VS. 465,000 BALES IN 1972/73. THUS, GROWERS FIND NEARLY THREE-QUARTERS OF THEIR EXPECTED CROP ALREADY COMMITTED AT PRICES WELL UNDER CURRENT MARKET LEVELS. MOREOVER, THE RECENT CURRENCY ADJUSTMENTS HAVE ADDED SHARPLY TO PRODUCTION COSTS AS JAPAN, GERMANY AND SWITZERLAND TRADITIONALLY SUPPLY A MAJOR SHARE OF NICARAGUA'S FERTILIZER AND PESTICIDE IMPORTS WHILE U.S. SUPPLIERS REPORTEDLY HAVE THEIR HANDS FULL WITH DOMESTIC REQUIREMENTS.

2. GIVEN THIS SITUATION, CENTRAL AMERICAN GROWERS ARE BECOMING INCREASINGLY RESTLESS AND U.S. BROKERS ARE BECOMING CONCERNED. THE CENTRAL AMERICAN COTTON PRODUCERS ASSOCIATION RECENTLY MET IN GUATEMALA TO CONSIDER PROPOSALS TO "RE-NEGOTIATE" FUTURES CONTRACTS WITH JAPAN. THE GROWERS PLAN TO SEND A DELEGATION TO JAPAN SHORTLY. MOST OF THESE CONTRACTS WERE WRITTEN BY U.S. BROKERS IN GUATEMALA AND NICARAGUA WHILE IN EL SALVADOR THE GROWERS' COOPERATIVE DEALS DIRECTLY WITH JAPANESE CUSTOMERS. ACCORDING TO MR. WILSON, THE JAPANESE ARE NOT LIKELY TO AGREE TO PRICE RE-NEGOTIATIONS. THUS, THE ALTERNATIVES OPEN TO THE GROWERS APPEAR TO BE GOVERNMENT INTERVENTION IN THE MARKET OR, FAILING

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THAT, WIDESPREAD NON-DELIVERY OF THE LOWER PRICED CONTRACTS.

3. OF THE TWO, GOVERNMENT INTERVENTION TO SET A RETROACTIVE MINIMUM EXPORT PRICE WOULD BE THE MOST ATTRACTIVE TO THE GROWERS AS IT WOULD SOLVE THEIR LEGAL PROBLEMS BY PERMITTING THEM TO PLEAD "FORCE MAJEURE". MR. WILSON CONCEDES THIS WOULD PROBABLY

ALSO FREE THE BROKERS FROM THEIR CONTRACTUAL OBLIGATIONS, BUT, HE BELIEVES, IT WOULD TOTALLY DISRUPT THE CENTRAL AMERICAN COTTON MARKETS AND END FUTURES CONTRACTS FOR YEARS TO COME. MR. WILSON SAID THAT, IN HIS JUDGMENT, GOVERNMENT INTERVENTION IS MOST LIKELY IN GUATEMALA WHERE PRE-ELECTION POLITICS MIGHT PLAY A ROLE AND LEAST LIKELY IN EL SALVADOR WHERE A FEW LARGE, SOPHISTICATED GROWERS DOMINATE THE TRADE. HE THOUGHT NICARAGUA WAS A QUESTION MARK.

4. NON-DELIVERY COULD ALSO CAUSE SERIOUS PROBLEMS IF IT BECAME WIDESPREAD BECAUSE OF THE SLOWNESS OF THE CENTRAL AMERICAN JUDICIAL SYSTEMS IN ENFORCING CONTRACTS. SHELTON

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C O N F I D E N T I A L FINAL SECTION OF 2 MANAGUA 3297

WIEL BROTHERS STILL HAS LAWSUITS OUTSTANDING IN NICARAGUA FOR NON-DELIVERY THREE YEARS AGO WHEN THE FUTURE/SPOT PRICE DIFFERENTIAL WAS ONLY \$4 PER CWT. IN STRICT CONFIDENCE WILSON SAID WIEL HAS TAKEN A NUMBER OF MEASURES TO PROTECT ITSELF AGAINST NON-DELIVERY

INCLUDING A LONG POSITION OF ABOUT 25 PERCENT (I.E. IT HAS CONTRACTED TO BUY 25 PERCENT MORE THAN IT HAS ACTUALLY SOLD); A CONSCIOUS EFFORT TO SIGN HIGHER PRICED CONTRACTS WITH THE SAME GROWERS WITH WHOM IT HAS THE LOWEST PRICED CONTRACTS; AND AN EXCHANGE OF CONTRACT INFORMATION AMONG LOCAL BROKERS TO REDUCE POSSIBILITIES FOR DUPLICATE SALES OF THE SAME COTTON. THE DEGREE OF SUCCESS OR FAILURE OF THESE MEASURES WILL NOT BE KNOWN UNTIL EARLY NEXT YEAR. IN THE MEANTIME, WIEL BROTHERS HAS STOPPED WRITING FUTURES CONTRACTS AND MR. WILSON, FOR ONE, HAS STARTED TAKING TRANQUILIZERS. UP TO THE PRESENT, WIEL BROTHERS HAS SOLD FUTURES CONTRACTS FOR 175,000 BALES OF CENTRAL AMERICAN AND MEXICAN COTTON TO JAPAN FOR A TOTAL CONTRACT VALUE OF
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OVER \$30 MILLION.

5. THE AMBASSADOR REPLIED THAT WE WERE AWARE, IN GENERAL TERMS, OF THE PROBLEM FROM PRESS REPORTS AND OUR DISCUSSIONS WITH COTTON GROWERS AND OTHERS. GENERAL SOMOZA HAD RECENTLY TOLD HIM THAT A DELEGATION OF CENTRAL AMERICAN COTTON GROWERS HAD ASKED THE GON TO INTERVENE TO BREAK THE EARLY CONTRACTS ALLEGING A POTENTIAL "LOSS" OF FOREIGN EXCHANGE EARNINGS OF \$30 MILLION FOR NICARAGUA AND \$100 MILLION FOR ALL OF CENTRAL AMERICA. THE GENERAL HAD REFUSED ON THE GROUNDS THAT THE ARBITRARY BREAKING OF CONTRACTS WOULD RAISE VALID QUESTIONS ABOUT THE RELIABILITY OF NICARAGUA AS A SUPPLIER AND ADVERSELY AFFECT LONGER TERM INTERESTS. THUS, THE AMBASSADOR SAID IT IS IMPROBABLE THAT THE GON WILL INTERVENE ON THE SIDE OF THE GROWERS. HOWEVER, HE SAID THE BROKERS SHOULD ALSO RECOGNIZE THAT THERE IS NOT MUCH THE GON CAN DO TO ENFORCE CONTRACRS. WILSON AGREED WITH THE LATTER AND SAID HE WAS NOT REQUESTING EMBASSY INTERVENTION AT THIS TIME BUT SIMPLY WANTED US TO BE AWARE OF THE PROBLEM.

6. COMMENT: WHILE WIEL BROTHERS POTENTIAL PROBLEMS ARE GREAT, THEIR PROFIT POTENTIAL ON THEIR LONG POSTION APPEARS COMMENSURATE. GIVEN THE SIZE OF THE STAKES, WE WOULD EXPECT U.S. BROKERS TO REQUEST VIGOROUS USG REPRESENTATIONS SHOULD IT APPEAR ONE OR MORE OF THE CENTRAL AMERICAN GOVERNMENTS WERE SERIOUSLY CONSIDERING INTERVENTION OR CONDONING NON-DELIVERY.
SHELTON

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